IN THE

Supreme Court of the United States

OCTOBER TERM, 1951.

No. 158.

THOMAS B. LILLY and HELEN W. LILLY, *Petitioners*,

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent*.

On Writ of Certiorari to the United States Court of Appeals for the Fourth Circuit.

REPLY BRIEF FOR THE PETITIONERS.

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PRESS OF BYRON S. ADAMS, WASHINGTON, D. C.

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The respondent's brief, we believe, has nicely confirmed the basic inadequacies of his position. In view of these inadequacies he anxiously urges an affirmance of the Tax Court's decision on a theory which he failed to disclose or intimate in that Court. (Resp. Br. 46.) For the convenience of the Court we would like briefly to note some of the deficiencies in the respondent's contentions.

1. The respondent's opening premise is that he who seeks a deduction must show a "clear provision therefor." (Resp. Br. 13.) We do not disagree with this statement of principle. However, the respondent's invocation of the principle has a peculiarly strange ring in this case. For it

is the respondent who has steadfastly ignored a "clear provision" of the Internal Revenue Code in order to apply a canon of deductibility emanating from beyond the Code. If one does not end with the words of a statute, "one certainly begins there." *Federal Trade Commission* v. *Bunte Bros.*, 312 U. S. 349, 350 (1941). Even tax law is no exception to this customary procedure in reading and applying statutes.

2. Although the respondent dwells at some length on the so-called doctrine of public policy, he fails to indicate the relevance of that doctrine in applying a statute which was simply designed to tax "commercial net income." "In law also the right answer usually depends on putting the right question." *Estate of Rogers* v. *Commissioner*, 320 U. S. 410, 413 (1943). Since the respondent has avoided "the right question," he has consistently assumed that Section 23(a)(1)(A) is a sanction directed against certain business expenses which are delusively defined in terms of "public policy." As a result, he spends a good deal of time on considerations which might be quite significant in a suit in equity, but are quite irrelevant in the calculation of an income tax. Cf. *Helvering* v. *Hallock*, 309 U. S. 106, 118 (1940); *Helvering* v. *Clifford*, 309 U. S. 331, 334 (1940). We are afraid that the respondent misses the essence of the matter. Section 23(a)(1)(A) implements and executes the fundamental principle of ability to pay by confining the tax to receipts less "ordinary and necessary" expenses. It makes no attempt to punish taxpayers by suspending the principle of ability to pay when the respondent feels that "public policy" may have been flouted. The statute hardly operates "in a vacuum," as the respondent pessimistically suggests (Resp. Br. 16), if it serves its own vital function and leaves other problems to other statutes.

Indeed, by ignoring the purpose of Section 23(a)(1)(A) the respondent has inevitably imposed a penalty rather than a tax. He has seen fit to punish the petitioners not

only "by taxing gross instead of net income" (cf. *Commissioner* v. *Heininger*, 320 U. S. 467, 474 (1943)), but by asserting a tax liability which far exceeds their net earnings. Specifically, for 1944 the respondent has imposed an aggregate tax of $49,577.88 with respect to a net profit of $25,280.06. (R. 3, 5, 199-200; Computation of Tax under Rule 50 in Tax Court.) Surely, in imposing a tax on "net income," Congress did not contemplate such bizarre and cruel consequences nor a tax rate which approaches 200 percent of earnings. Even a fraud penalty does not exceed 50 percent of a tax deficiency. Internal Revenue Code § 293(b).

3. The respondent scarcely explains away the illuminating legislative history of 1913. (Resp. Br. 25.) That history emphasizes that in allowing deductions for "expenditures or losses" Congress was not concerned with approving or disapproving business outlays on moral grounds.[1] The respondent weakly suggests that in failing to legislate Congress necessarily adopted some principle of public policy as variously applied in the lower courts.[2] As this Court wisely observed in *Scripps-Howard Radio* v. *Commission*, 316 U. S. 4 (1942), "The search for significance in the silence of Congress is too often the pursuit of a mirage. We must be wary against interpolating our

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[1] In this connection the respondent states that an "expense," as distinguished from a "loss," must be "ordinary" and "necessary." We do not understand how this distinction helps the respondent in ignoring the legislative history or in applying a principle of public policy to expenses which are otherwise "ordinary" and "necessary."

[2] The respondent seems to say that a full-fledged doctrine of public policy has been judicially established for thirty-eight years. The first appellate decision recognizing an isolated aspect of the doctrine did not appear before 1930. *Great Northern Railway Co.* v. *Commissioner*, 40 F. 2d 372 (C. A. 8, 1930), *cert. denied*, 282 U. S. 855 (1930). Since then the doctrine has had a tortuous career in the courts. See Pet. for Cert. p. 14 *et seq.*; Pet. Br. p. 15 *et seq.* And in *Commissioner* v. *Heininger*, *supra*, this Court disapproved a good deal of the public policy doctrine as understood by the respondent. Pet. Br. p. 24.

notions of policy in the interstices of legislative provisions." *Id.* at p. 11. "To explain the cause of non-action by Congress when Congress itself sheds no light is to venture into speculative unrealities." And "we walk on quicksand when we try to find in the absence of corrective legislation a controlling legal principle." *Helvering* v. *Hallock, supra,* at pp. 119-121.[3] In regard to its own decisions this Court has stated, "It would require very persuasive circumstances enveloping Congressional silence to debar this Court from reexamining its own doctrines." 309 U. S. at p. 119. Certainly this Court is at least equally free to appraise a disorderly doctrine which has sporadically evolved in the lower courts—especially if the doctrine has been insensitive to Congressional policy and is inevitably creating a quagmire of confusion. Cf. *Higgins* v. *Smith,* 308 U. S. 473, 478 (1940); *Neirbo Co.* v. *Bethlehem Corp.,* 308 U. S. 165, 174 (1939).[4] In the words of Judge Learned

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[3] See further *United States* v. *Underwriters Assn.,* 322 U. S. 533, 559 (1944); *Girouard* v. *United States,* 328 U. S. 61, 69 (1946); and concurring opinion of Rutledge, J., in *Cleveland* v. *United States,* 329 U. S. 14, 21 (1946).

[4] As the respondent has pointed out, Congress acted in 1934 within the restricted area of wagering losses by disallowing such losses to the extent that they exceeded wagering gains. Revenue Act of 1934, c. 277, 48 Stat. 680, Sec. 23 (g). The same rule is now incorporated in Section 23(h) of the Internal Revenue Code. When Congress enacted the provision, it had been held that losses in illegal gambling transactions were deductible only to the extent of gains in similarly illegal transactions. At the same time losses from legal gambling transactions were fully deductible. However, it appeared that "many taxpayers" would "take deductions for gambling losses but fail to report their gains." Hence Congress limited the deduction of losses in order to "force taxpayers to report their gambling gains if they desire to deduct their gambling losses." H. R. Rep. No. 704, 73d Cong., 2d Sess. (1934) 22; Sen. Rep. No. 558, 73d Cong., 2d Sess. (1934) 25. In brief, the 1934 amendment merely sought to limit the deduction of all gambling losses as a means of preventing a specific kind of tax evasion. The objective of the provision was not to penalize gambling, but to safeguard the integrity of the tax system.

Hand, "To suppose that Congress must particularly correct each mistaken construction under penalty of incorporating it into the fabric of the statute appears to us unwarranted; our fiscal legislation is detailed and specific enough already." *F. W. Woolworth Co.* v. *United States*, 91 F. 2d 973, 976 (C. A. 2, 1937), *cert. denied*, 302 U. S. 768 (1938).

4. The respondent makes the astonishing assertion that an expense is not "ordinary" unless "it conforms to the standards of the business community as a whole" rather than the norms of the particular trade. (Resp. Br. 57.) This Court has articulated a somewhat different view. The basic criterion of "ordinary" is "normalcy in the particular business." See *Deputy* v. *du Pont*, 308 U. S. 488, 495-496 (1940). See also 4 Mertens, The Law of Federal Income Taxation, p. 317 (1942). As Mertens felicitously puts it, "The test may well be said to be what the average hardheaded businessman would have done under like circumstances." *Id.* at p. 319.

The respondent makes a related statement which is similarly surprising. He insists that payments to physicians were not ordinarily made in the industry. (Resp. Br. 56.) Since this matter was discussed in our original brief (p. 29 *et seq.*), we consider it inappropriate to explore anew the same ground. We would like to note, however, that in 1946 the Government publicly declared that the practice was "industry wide." (*Id.* at p. 31.) Apparently for the purposes of this case the Government prefers to suggest that the facts were otherwise.

5. The respondent apparently misunderstands the petitioners' position. According to the respondent, the petitioners are supposedly arguing that "Section 23(a)(1)(A) is concerned solely with net income, so that any denial of deduction for an expense actually paid or incurred contravenes the statute." (Resp. Br. 23.) On the basis of this misapprehension the respondent then replies that the al-

leged argument "ignores the fact that Congress did not authorize deduction of every business expense paid or incurred, but only of such expenses paid or incurred as were 'ordinary and necessary.'" *Ibid.* The respondent has methodically answered an argument which the petitioners have not made. The petitioners readily agree that an expense must be both "ordinary and necessary" in order to be deductible. Since the outlays involved in this case qualified as "ordinary and necessary," the petitioners contend that the respondent has erred.

6. The respondent urges this Court to "pay great deference to the expert judgment of the Tax Court." (Resp. Br. 14-15.) Of course, as the respondent is undoubtedly well aware, his own "deference" is quite flexible. It varies from case to case, depending on whether the Tax Court happens to agree with him. For a few recent examples, see *Crane* v. *Commissioner*, 331 U. S. 1 (1947); *Commissioner* v. *Estate of Church*, 335 U. S. 632 (1949); *Commissioner* v. *Korell*, 339 U. S. 619 (1950). At present we need not dwell at length upon the respondent's elastic notions of "deference" as they are regularly reflected in the cases. The Tax Court's conclusion in this case did not derive from an "expert judgment" representing an accretion of technical tax wisdom. See *Trust of Bingham* v. *Commissioner*, 325 U. S. 365 (1945). Moreover, here as in *Commissioner* v. *Heininger, supra,* at pp. 470, 475, the Tax Court "denied the claimed deduction not by an independent exercise of judgment but upon a mistaken conviction that denial was required as a matter of law." It did not act "upon its own interpretation of the words 'ordinary and necessary,'" but under the supposed compulsion of an appellate decision. (R. 180.)

7. The respondent argues rather emphatically that the payments to the doctors artificially raised the retail price of glasses by one-half of what the price would otherwise be. (Resp. Br. 48.) There is no evidence in the case to

sustain this conclusion. Obviously a price structure is determined by much more than one isolated cost factor. However, even if we indulge in the respondent's gratuitous assumption, we fail to understand the significance of his argument. The purpose of Section 23(a)(1)(A) is not to control or limit prices. Moreover, if the respondent's factual assumption is correct, in the absence of payments to physicians, the customers would have paid a price which was one-third less than the price actually paid. Therefore, the petitioners would have had a net profit equal to their actual net profit in this case. Yet their tax would have accordingly been less than the tax now asserted by the respondent, though their profit would have been precisely the same. Or to state the matter differently, the respondent is, in effect, adding a penalty, because the petitioners made payments to the physicians.

8. In his effort to sustain his conclusion the respondent is compelled to indulge in exaggeration. For example, he cites the Restatement on Restitution for the proposition that under "established rules of contract, agency and trust, the patients could have recovered the rebates" from the petitioners. (Resp. Br.)[5] There is nothing in respondent's reference which ratifies his view that a customer could have recovered from the petitioners any related amount which they had already paid to the physicians. In that context the petitioners would not be unjustly enriched, nor would they be withholding a "benefit" which should be restored to the "beneficiary." On the other hand, if we assume that a customer were able to recover the same amount from the petitioners before it was paid to the physician, the amount of the recovery would be clearly deductible as a business

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[5] Section 138 of the Restatement on Restitution states that a "third person who has colluded with a fiduciary in committing a breach of duty, and who obtained a benefit therefrom, is under a duty of restitution to the beneficiary."

expense, as even the respondent seems to concede. (Pet. Br. 19-20; Resp. Br. 55.)[6]

9. The respondent is not disinclined to mention irrelevancies. To illustrate, he mentions two criminal statutes which have nothing to do with this case. To quote the respondent, these statutes provide that "the giving of consideration to an agent with intent to influence his action in relation to his principal's business constitutes a misdemeanor." (Resp. Br. 35.) These two statutes have no bearing here and must have been imported into the case solely for atmospheric purposes.[7] Obviously a physician is not the agent of his patient, and a patient does not engage in business by purchasing glasses.

10. The respondent misconstrues this Court's decision in *Textile Mills Corp.* v. *Commissioner*, 314 U. S. 326 (1941). He erroneously assumes that the decision embraced the vagrant doctrine of public policy which he espouses. In that case the Court considered the validity of a regulation which denied the deduction of any sums "expended for lobbying purposes." See *id.* at p. 337, n. 16. The regulation made no mention of public policy and did not distinguish between legitimate lobbying contracts and the illegiti-

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[6] From a tax standpoint it seems odd to say, as the respondent in effect argues, that petitioners could have deducted any amounts paid back to their customers, but may not deduct any amounts paid to the doctors, from whom the customers could have recovered. In both cases the seller's gain on the sale is exactly the same.

[7] The evidence in no way supports the respondent's assertion that the petitioners "camouflaged" their payments to the doctors. The payments were clearly classified as "trade discounts" on the petitioners' books and tax returns, and the petitioners made no attempts to conceal the "discounts" and payments. (R. 21, 22, 121-123, 161-175.) The doctors were clearly identified on the petitioners' books, and the payments made to them were unmistakably shown. (R. 21, 88, 90, 94, 96-97, 101-102, 104, 117, 118, 121, 164-175.) The Tax Court conceded "that the petitioners reasonably believed that the deduction was proper in computing income," and that "there was no concealment as to the amount of the deduction." 14 T. C. at 1086.

mate variety. It determined rather that lobbying expenses, regardless of their nature, are not ordinarily and necessarily incurred in the conduct of a business. But cf. *McGarry* v. *Limerick Gas Committee*, [1932] Ir. R. 135, allowing the deduction of lobbying costs as business expenses.

In sustaining the regulation the Court stated that the "words 'ordinary and necessary' are not so clear and unambiguous in their meaning and application as to leave no room for an interpretative regulation." The Court then pointed out that the Treasury, in the exercise of its "rule-making authority," might reasonably determine that expenses of lobbying are not "ordinary and necessary," whether or not the expenses in a particular case are incurred under a fully enforceable contract. Therefore, the Court considered it wholly immaterial whether the precise arrangement involved in the case "would violate the rule" which outlaws certain lobbying contracts. See *Textile Mills Corp.* v. *Commissioner*, *supra*, at pp. 338-339. See further *Sunset Scavenger Co.* v. *Commissioner*, 84 F. 2d 453 (C. A. 9, 1936), where the Ninth Circuit similarly sustained the regulation as a not unreasonable interpretation of "ordinary and necessary," though the Tax Court considered the expenses involved as entirely "legitimate."

In this case, as in the *Heininger* case, "we do not have the benefit of an interpretative departmental regulation defining the application of the words 'ordinary and necessary' to the particular expenses here involved." See 320 U. S. at p. 470. See further Pet. Br. 21, n. 19. For that matter, here the Treasury has made no attempt whatsoever to define what is "ordinary" and "necessary" in the light of "common or frequent occurrence in the type of business involved." See *Deputy* v. *du Pont*, *supra*, at p. 495.[8] Instead the respondent has ignored the concepts of "ordi-

[8] Lobbying expenses are susceptible to a more generalized treatment, for by and large there are no serious industry variations in practice.

nary" and "necessary" in order to deny a deduction on the basis of public policy. Needless to say, the respondent is not an expert in the realm of public policy nor is his conclusion here based on any expert knowledge of tax law. This Court has indicated that even regulations are not particularly authoritative where they "do not embody the results of any specialized departmental knowledge or experience." *Haggar Co.* v. *Helvering*, 308 U. S. 389, 398 (1940). This appraisal of the Treasury's administrative wisdom is *a fortiori* applicable here, for not even a regulation is involved and the respondent has stepped much beyond his limited area of "superior knowledge." *Estate of Sanford* v. *Commissioner*, 308 U. S. 39, 53 (1939).

11. In order to sustain the asserted deficiencies the respondent resorts to a theory which admittedly "was not urged in the Tax Court."[9] On appeal the respondent devoted two pages to this new theory,[10] which the Court of Appeals considered too trivial to mention. The respondent's new theory, as we understand it, is that the payments in question are not deductible because they constituted violations of the Sherman Act. (Resp. Br. 46.) In support of this position the respondent refers to a complaint in an anti-trust suit and a consent judgment to which neither petitioner was a party.

As the respondent himself evidently concedes, the decision of a lower court may not be sustained on a new legal theory where "facts not already of record are required for decision." (Resp. Br. 49, n. 20.) It is "familiar appellate procedure" that if the correctness of a lower court's deci-

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[9] Resp. Br. 49, n. 20.

[10] Resp. Br. in Ct. of App. 35-36. This was not the first time that a new theory appeared in the case for the benefit of the respondent. In the Tax Court he did "not argue" that the payments "were contrary to public policy." Instead he argued that the payments were "not ordinary and necessary expenses in that they were voluntary and incident to an unethical practice." (R. 199.)

sion hinges on a determination of fact which only that court "could make but which has not been made," the appellate court cannot take the place of the trial court. See *Securities Commission* v. *Chenery Corp.*, 318 U. S. 80, 88 (1943).[11] This Court explained in *Hormel* v. *Helvering*, 312 U. S. 552, 556 (1941), that "our procedural scheme contemplates that parties shall come to issue in the trial forum vested with authority to determine questions of fact. This is essential in order that parties may have the opportunity to offer all the evidence they believe relevant to the issues which the trial tribunal is alone competent to decide; it is equally essential in order that litigants may not be surprised on appeal by final decision there of issues upon which they have had no opportunity to introduce evidence."[12]

There is not the slightest evidence in this case that the petitioners violated the anti-trust laws in making payments to physicians. As the respondent's argument indicates, the anti-trust laws are directed against conspiracies to fix prices. They are not concerned with rebates unless the rebates are an integral element in a plan to fix prices. This view is plainly reflected by the complaint against the American Optical Company upon which the respondent now strangely relies. The gravamen of this complaint was that the American Optical Company and certain doctors, *not these petitioners*, had entered into a conspiracy to fix the price of spectacles.

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[11] See also *Bondholders Committee* v. *Commissioner*, 315 U. S. 189, 192 (1942); *LeTulle* v. *Scofield*, 308 U. S. 415, 421 (1940); *General Utilities Co.* v. *Helvering*, 296 U. S. 200, 206 (1935); *Anderson* v. *Commissioner*, 156 F. 2d 591, 593 (C. A. 2, 1946); *Legg's Estate* v. *Commissioner*, 114 F. 2d 760, 766 (C. A. 4, 1940).

[12] In the *Hormel* case itself a new theory was considered on review because of "exceptional circumstances"—an intervening decision by this Court. However, even in those unusual circumstances this Court remanded the case to the trial court in order to permit new evidence to be introduced on the new issue.

The complaint alleged that American Optical was one of the two largest manufacturers and wholesalers of ophthalmic goods in the United States. In addition, American Optical was itself engaged in the retailing of spectacles to the public. The Government charged that American Optical had conspired with a number of physicians to sell glasses to patients at a price which would be "at least as high as the local prevailing consumer prices charged by optometrists and retail opticians for spectacles" of "equivalent quality." American Optical sought to preserve this price level, the Government declared, in order "to maintain the good will of optometrists and retail opticians" who were its customers as well as its competitors in the retail area. As a part of the plan to maintain prices at the desired level and to obtain the cooperation of the doctors to this end,[13] American Optical allegedly agreed to pay physicians a portion of the retail price if they referred patients to the Company. (R. 202-220.)

We are wholly unable to understand the relevance of the American Optical complaint in this case. In the first place, the petitioners were not parties to the suit. Secondly, the complaint was directed against price-fixing and not rebates as such. Thirdly, there is absolutely no evidence in this case that the petitioners made any attempt to fix competitive prices or that their payments to doctors were directed toward this end. The competitive situation of the petitioners was utterly dissimilar to the position of American Optical. The petitioners could not have fixed prices even if they had wished to do so. They were, in fact, the victims of American Optical's activities. For that Company was

[13] The American Optical plan sought to prevent price cutting by refusing to sell to the patient of any doctor who passed on to his patient any part of the rebate, thus indirectly reducing the price to the patient. (R. 212, 214.) There is no suggestion in this record that these petitioners followed any such policy.

the petitioners' principal competitor (R. 17, 74, 77, 111, 125, 129, 134-135, 146, 150, 152-153, 157) and was finally enjoined from making rebates on May 16, 1951. (Resp. Br. 83-92.)

American Optical was a giant concern in the industry. Unlike the petitioners, it carried on a tremendous trade with opticians and optometrists as well as consumers. (R. 208-209.) The Company had 254 wholesaling branches in 47 states, the District of Columbia and Hawaii. (R. 207.) It allegedly made payments to as many as 3,000 doctors. (R. 204-205.) In 1944 and 1945 its aggregate payments to only 22 doctors amounted to $277,676.38. (R. 221.) American Optical usually paid doctors one-half of the consumer price. (R. 210, 212-217.) However, payments varied, and representative transactions included a payment of $11.50 where the consumer price was $14. (R. 219.) While it may have been in the interest of American Optical to fix prices because of its peculiar relation to competitors, it is gratuitous to suggest that the petitioners violated the anti-trust laws because American Optical may have done so. We should also add that the attempt to attribute to one person the alleged guilt of another, without the least semblance of a trial, is a substantial innovation in prevailing concepts of due process.[14]

12. In our prior brief (p. 31 *et seq.*) we stated that the respondent's notion of public policy is unembarrassed by noticeable limitations. Nothing in the respondent's brief

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[14] Even one who is charged with an anti-trust violation can be punished "only in a judicial proceeding in which the accused has the benefit of constitutional and statutory safeguards appropriate to trial for a crime." Cf. *Commissioner* v. *Heininger, supra,* at p. 474. In fact, here, as distinguished from the *Heininger* case, the respondent would attach "a serious punitive consequence" *to his own administrative finding* in a field far beyond taxation. Although both petitioners testified in this case (R. 7, 82), the respondent made no inquiry concerning an alleged violation of the anti-trust statutes, nor did he seek any information on the petitioners' connection with interstate commerce.

suggests that serious limitations are in sight. The respondent assures the Court that he possesses an "informed discretion" which enables him to discriminate wisely in supervising "every form of commercial practice" on an *ad hoc* basis. (Resp. Br. 53.) One need not be very imaginative in suggesting how that "informed discretion" would operate in the name of "public policy."

For example, "there is authority to the effect that a bargain to buy goods which to the buyer's knowledge the seller was under contract to sell to another" is contrary to public policy. Williston, The Law of Contracts, p. 4908 (Rev. ed. 1938). Therefore, the respondent would feel free to disallow the deduction of all expenses incurred in obtaining the bargain.[15] "A bargain of employment which to the knowledge of the parties violates an existing contract with another has been held invalid." *Id.* at p. 4910. Hence in the name of public policy the respondent would disallow the deduction of compensation paid under the later agreement. In a number of states an unlicensed foreign corporation cannot recover on its contracts, which are considered contrary to public policy. *Id.* at p. 5029. Evidently under the respondent's view expenses incurred by the corporation in connection with such contracts would not be deductible. Again, many state statutes, articulating a well-defined and traditional public policy, have long condemned contracts made or to be performed on Sundays. *Id.* at pp. 4824, 4831-4832; 6 Corbin, Contracts, p. 886 (1951). If the respondent is correct, a businessman would be deprived of a deduction for expenses incurred in the execution of such contracts.[16]

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[15] Very likely the respondent would consider himself equally free to ignore the cost of the goods in computing the purchaser's gain on a resale. Cf. I. T. 3724, C. B. 1945, p. 57.

[16] Indeed, where a taxpayer is engaged in numerous interstate transactions, the Government's view requires the transactions to be identified and dated state-by-state, in order to prevent deductions against "public policy." There might be considerable difficulty in determining the applicable state law.

We have already noted (Pet. Br. 28, n. 26) that even the respondent is confused in applying his principle of public policy. For random additional examples, see *Commissioner v. Heininger, supra; Jerry Rossman Corporation v. Commissioner*, 175 F. 2d 711 (C. A. 2, 1949). The respondent's brief fortifies this conclusion.[17] The respondent indicates that a taxpayer may not deduct any payment to an agent which is designed to influence the latter's services in behalf of his principal. (Resp. Br. 35.) At the same time, however, he evidently concedes the correctness of the decision in *F. L. Bateman*, 34 B. T. A. 351 (1936), where tips were paid so that the payee would favorably influence his principal. (Resp. Br. 54.) We are not implying that the *Bateman* case was wrongly decided. We are simply pointing out that the respondent easily gets lost in the obscurities of public policy.

The respondent's confusion reinforces Judge Arundell's warning that courts "should be reluctant to undertake the determination of the question of what is and what is not contrary to public policy, both for the United States and for each of the 48 states, where the act condemned as against public policy is not one shown to be in violation of any law of the land. What are deductible items should be known to a taxpayer with reasonable certainty under our income tax system." (R. 199.)

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[17] The respondent cites two English cases (Resp. Br. 22, n. 6), which do not tell the entire story. In those two cases deductions for penalties were disallowed because under the peculiarities of the English law they were not regarded as "in the nature of a commercial loss." The decisions did not rest on "public policy." Moreover, a basic distinction between English law and our law is that in England no deduction is allowed for damages paid because of a wrong committed in the operation of a business. *Strong & Co. v. Woodifield*, [1906] A. C. 448.

The respondent has unintentionally illustrated an incisive observation made many years ago by an English jurist. Public policy "is a very unruly horse, and when once you get astride it you never know where it will carry you. It may lead you from the sound law. It is never argued at all but when all other points fail." *Richardson* v. *Mellish*, 2 Bing. 229, 252 (Com. Pl. 1824).

Respectfully submitted,

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